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In The

Supreme Court of the United States

Term, 1971

No. 71–61

NATHAN WECHSLER,

Petitioner,

vs.

IRVING GOTTLIEB et al.,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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Counterstatement of the Question

Where the United States Court of Appeals reversed the judgment of the District Court as to a corporate defendant finding that the corporate defendant was not properly served but affirmed the District Court's judgment against an individual defendant in an action brought under the fraud provisions of the Federal Securities Law, is the judgment against the individual defendant a valid one?

Counterstatement of the Case

Respondents were owners of securities of World Wide Bowling Enterprises, Inc., a Delaware corporation (hereinafter referred to as "World Wide"). The action was brought under the fraud provisions of the Securities and Exchange Act of 1934, as amended, 15 U.S.C.A., Sec. 18(a) et seq., Section 10(b) and Rule 10(b)-5, 17 C.F.R. 240, 10(b)-5 adopted by the Securities Exchange Commission, and the Securities Act of 1933, as amended, 15 U.S.C.A. Sec. 77(a) et seq.

The action arose when the stockholders and debenture holders agreed to sell their World Wide stock to Sandia American Corporation (hereinafter referred to as "Sandia"), one of the defendants below, the purchase price being shares of Sandia which thereby acquired all of the assets of World Wide. Petitioner, Nathan Wechsler, who was a practicing attorney and certified public accountant in the District of Columbia was also the negotiating agent and the controlling stockholder of Sandia, acted as both counsel and accountant for Sandia and who, in general, was the moving force behind the transaction.

The other named defendants below were officers and directors of Sandia. The acts complained of created a pattern of both general and specific acts of omission and commission on the part of Sandia, petitioner, Nathan Wechsler being the moving party. One of the specific acts alluded to by the District Court and the United States Court of Appeals concerns Sandia's execution of $784,000 in promissory notes to a third corporation which was not reflected in the Sandia Finan-

cial Statement or otherwise communicated to respondents prior to consummation of the agreement, and that there was, therefore, a misrepresentation of the true value of the Sandia stock at the time they agreed to take it in exchange for their World Wide holdings. By order dated April 14, 1970, the District Court sustained a report by a Special Master which awarded to respondents $50,000 plus 6% interest annually. On appeal, the United States Court of Appeals for the Third Circuit reversed the judgment of the District Court as to the corporate defendant in an opinion filed March 15, 1971 finding that the corporate defendant was not properly served but affirmed the District's Court's judgment against Nathan Wechsler, the individual appellant, the petitioner herein.

It is the petitioner's position that the corporate defendant was an indispensable party to the suit and that the judgment against him should not stand. The respondent's position that liability is not limited to the corporation but extends also to any person associated with the corporation who withholds material information, in this case concerning the value of Sandia's stock.

Reasons for Denying the Writ

LIABILITY IS NOT LIMITED TO THE CORPORATION (SANDIA) BUT EXTENDS ALSO TO ANY PERSON (PETITIONER) ASSOCIATED WITH THE CORPORATION WHO WITHHOLDS MATERIAL INFORMATION CONCERNING THE VALUE OF THE CORPORATION'S STOCK.

The lower court held that there was a failure on the part of the officers and directors of

Sandia to disclose material facts relating to Sandia's financial statements, to the general financial condition of Sandia, its subsidiaries and its owners, to the details of the contractual arrangements with a third corporation for the purchase and operation of bowling centers, to the uncertainty and remoteness of profit to Sandia under such arrangements, and to the other potential liabilities to Sandia or its subsidiaries arising from the contract; and the failure of the defendants to make the World Wide share and debenture-holders aware of these facts prior to the consummation of the acquisition of World Wide by Sandia constituted violation of Rule 10(b)-5 for which the defendants (of which petitioner was one) may be held liable for damages. The court cited: Kardon v. National Gypsum Co., 73 F. Supp. 798 (E.D. Pa. 1947); Royal Air Properties, Inc. v. Smith, 312 F.2d 210 (9th Cir. 1962); Heit v. Weitzen, 402 F.2d 909 (2nd Cir. 1968); Myzel v. Fields, 386 F.2d 718 (8th Cir. 1967), cert. denied 390 U.S. 951 (1968); Stevens v. Vowell, 343 F.2d 374 (10th Cir. 1965); Mader v. Armel, 402 F.2d 158 (6th Cir. 1968). The District Court also referred to Bromberg, Securities Laws: Fraud — SEC RULE 10b-5, Section 4, 2, p. 69 (1969) and cases therein cited.

The United States Court of Appeals in this case irrefutably held that the correctness of the judgment against the individual appellant (petitioner) turns on the validity of the District Court's finding of the violation of Section (b) of Rule 10(b)(5), 17 C.F.R. Sec. 240, 10b-5:

"It shall be unlawful for any person...

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading...."

The court below in its opinion filed March 15, 1971, Circuit Judge Aldisert stated:

> "The Court found a misstatement or omission of material fact in a December 31, 1961, consolidated financial statement of Sandia American Corporation. The Corporation, princpally through Wechsler, acquired assets of World Wide Corporation in exchange for Sandia American stock. Plaintiff-appellees, formerly stock and debenture holders of World Wide, alleged that Sandia American's execution of $784,000 in promissory notes to a third corporation was not reflected in the financial statement or otherwise communicated to them prior to consummation of the agreement, and that there was, therefore, a misrepresentation of the true value of the Sandia American's stock at the time they agreed to take it in exchange for their World Wide holdings" (p. 28, Appendix — Opinion). (Underlining added.)

The United States Court of Appeals in upholding the violation by the appellants below stated "the test is satisfied 'whenever a device was employed of a sort that would cause reasonable investors to rely thereon, and, in connection therewith, so relying, cause them to purchase or sell a cor-

poration's securities. SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 860 (2 Cir. 1968)'" (p. 30, Appendix-Opinion). That court also cited: Heit v. Weitzen, supra; City National Bank v. Vanderboom, 422 F.2d 221, 229 (8 Cir. 1970); SEC v. North American Research and Development Corp., 424 F.2d 63, 82 (2 Cir. 1970); Royal Air Properties, Inc. v. Smith, supra.

Judge Aldisert's opinion then, simply and succinctly held that liability is not limited to the corporation but extends to any person associated with the corporation who withholds material information concerning the value of the corporation's stock. 15 U.S.C. Sec. 78(b); 17 C.F.R. Sec. 240, 10b-5.[1] Quoting directly from the opinion:

> "Appellant Wechsler was the negotiating agent for Sandia American in the transaction with plaintiffs. He was the senior partner of the accounting firm which prepared the consolidated financial statement of Sandia

1. Rule 10(b)(5), 17 C.F.R. §240.10b-5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud.
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

> American and subsidiary companies, the controlling stockholder of the parent corporation, and a partner in Star Associates, the operating company for Sandia American's subsidiaries. His actions clearly came within the pale of the regulation and the statute" (p. 30, Appendix-Opinion).

In the light of Judge Aldisert's specific holding that petitioner is liable, in personam, it is difficult to comprehend petitioner's contention that the verdict below cannot stand. To preclude liability on the ground that the corporation was an indispensible party runs counter to the spirit, the rationale and the simple language of the regulation and the statute each of which aims its protective thrust against individuals associated with a corporation who withhold material information concerning the value of the corporation's stock. Both the District Court and the United States Court of Appeals name this petitioner as one who in this case knowingly withheld material information from respondents concerning the value of Sandia's stock.

The decision of the Third Circuit in this case is clearly in line with the decisions of this Court and the cited Circuit Courts which hold corporate insiders personally liable for their misleading acts of omission and commission; in the giving of misleading information and the withholding of pertinent information concerning the value of the corporate stock. The cases cited by the petitioner are not mundane to the subject matter of this case.

Conclusion

For these reasons, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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